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INTERVIEW

Non-linear growth: The road ahead for Indian IT outsourcing companies

The Infosys experience: In conversation with S. Gopalakrishnan, CEO and MD, Infosys Technologies

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HCL

Abstract Indian IT outsourcing companies (major among them being the SWITCH companies - Satyam, Wipro, Infosys, TCS, Cognizant and HCL) grew rapidly for more than a decade on low cost business process and IT outsourcing. With the bigger companies already reaching a high of 100,000 employees, they are now turning their attention to non-linear revenue (i.e. revenue less dependent on numbers or greater revenue earned per employee). For this they need to pursue 'disruptive' strategies which are distinctly different from the 'incremental' initiatives they adopted in the past to maintain linear revenue. This paper first outlines the disruptive and the incremental initiatives of the SWITCH companies and the road ahead for them. This is followed by an interview with S Gopalakrishnan, CEO and MD, Infosys Technologies who discusses the non-linear initiatives of the company and the challenges it faces in the field.

Changes wrought by organisational initiatives can be categorised as 'disruptive' (Christensen, 1997) or incremental. 'Disruptive' changes change the way products and services compete in the market. To give an example, videoconferencing reduces the need for travel. However the underlying technologies of travel and videoconferencing are not the same. But they compete with each other because they both address the same basic need, i.e. to communicate and conduct business. Tushman and Anderson (1986) call them radical innovations. Incremental changes are those that enhance or better the performance of an existing technology or product. For example, a Pentium chip is ahead of a 486, though both have the same design philosophy and are from the same firm. Literature on disruptive and incremental innovation focuses on technology. However the concepts of disruptive and incremental change can be applied to almost any aspect of an organisation. This article applies them to the realm of strategy, marketing and organisational initiatives. There are firms that adopt incremental initiatives and there are others that adopt disruptive initiatives. More often than not firms adopt both these approaches because incremental initiatives answer today's needs and disruptive initiatives answer tomorrow's.

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Indian IT outsourcing companies have been doing a bit of both. When they shot into the limelight, a decade ago, they were seen by several Fortune 2000 companies as a smart way of cost saving. They earned the acronym SWITCH (Satyam, Wipro, Infosys, Tata Consultancy Services (TCS), Cognizant and HCL). Of these TCS, Infosys and Wipro are the bigger ones, with Cognizant rapidly closing the gap (http://articles.timesofindia.indiatimes.com). Today, however, after a period of unprecedented growth they face the question: Will the future be the same as the past? Or will it be different? In the past they grew by increasing their head count and earning revenues proportional to the number of employees. The bigger among them already have more than one hundred thousand employees. Infosys earns $46,352 per employee while TCS earns $43,379 per employee (economictimes). How far can this growth proportional to the number of employees continue? This is pushing them to look at non-linear growth, i.e., earning more revenue per employee. To map it to what we discussed in the beginning, while incremental initiatives gave them steady growth so far, is the future in the realm of disruptive initiatives? That discussion forms the basis of this paper.

SWITCH companies are initiating up several incremental and disruptive initiatives. Some of those initiatives are listed in Fig. 1 and Fig. 2 below. It may be noted that the same generic initiative can be implemented differently making it either incremental or disruptive.

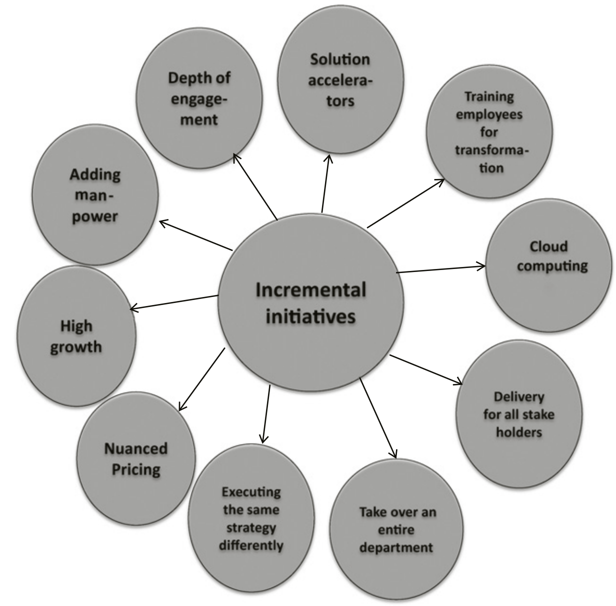

Fig. 2 Incremental Initiatives of Indian IT Outsourcing Companies.

Initiatives for incremental growth

Rapid growth

Rapid growth is in itself a mechanism of maintaining a gap between the firm and its competition (Bhattacharya and Michael, 2008). The SWITCH companies' growth was assisted by an English speaking and relatively low wage force, technical education and proactive government policy besides the large number of Indian employees working in Silicon Valley (Srinivasan, 2005). Morgan, Kaleka and Katsikeas (2004) show that a firm's performance in foreign markets depends directly on resources and capabilities, but less directly on competitive intensity. SWITCH companies have been growing more rapidly than others because they saw the potential of the outsourcing market before the others and built capabilities to deliver growth. TCS was involved in the IT services business right from 1968 (www.nasscom.com). Infosys, the other well known Bangalore based firm, was incorporated in 1981 (www.infosys.com). HCL initially started with the idea of offering IT products in the year 1976 (www.hcltech.com). Wipro set for itself the ambitious target of 4-in-4, that is, 4 billion dollars by 2004 (Hamm, 2007). Thus the SWITCH companies had a head start vis-à-vis smaller Indian and other IT outsourcing companies. They managed to get a critical mass of clients before the others and grew over a period of several years. Recent results also confirm this. Mid level IT firms like Mastek, MindTree and Mphasis have not been able to deliver the results that the SWITCH companies delivered (smartinvestor; www.makemystocks.com; www.moneycontrol.com). Early high growth is one of the reasons why the SWITCH companies are much ahead of their smaller competitors.

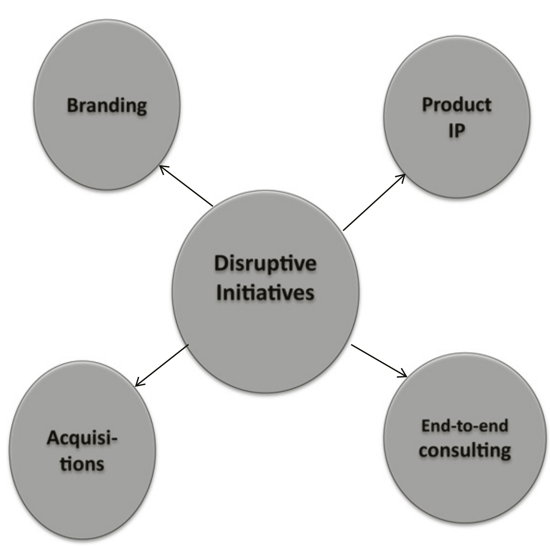

Fig. 1 Disruptive Initiatives for Growth by Indian IT Outsourcing Companies.

Adding man power

SWITCH companies are actively working on three aspects of manpower planning, namely, number,quality and retention. They have built commendable scale over a period of time by recruiting in large volumes. (TCS's recruitment of 1075 students from the batch graduating in 2009 from VIT University has entered the Limca Book of Records (www.hindu.com). Recruitment is followed by training to match the expectations of customers. With experience goods such as services, employees are expected to have basic skills but are expected to be tuned to customer delight, are trained to perform tasks of medium complexity and the specialists among them are expected to have a reasonable knowledge of the adjacent domains (Moorthi, 2002). Zeithaml and Bitner (1996) call the frontline employees in any service 'boundary spanners' (Zeithaml & Bitner, 1996). Both the image and the delivery of a service depend crucially on boundary spanners. Research also confirms that customer focus and organisational citizenship behaviour leads to customer satisfaction which in turn leads to sales (Schneider, Ehrhart, Mayer, Saltz, & Niles-Jolly, 2005). Thus the quality of service personnel is the key to the success of a service firm. Chandrasekharan, President and MD, Cognizant Technology Solutions (one of the SWITCH firms) feels that while quantity is not a problem, quality of personnel available is an issue. The company runs a training academy to address this issue besides conducting job fairs and recruiting from institutes like the Board of Apprenticeship Training (www.financialexpress.com/..../197942/). SWITCH companies are also working on retention. Attrition levels grow as economies grow and opportunities multiply. Infosys is planning to circulate the jobs and compensations available in an internal job market to provide choice to employees (http://in.ibtimes.com). Wipro is restructuring its hierarchy and giving restricted stock options (www.financialexpress.com/...../705699/). Thus working on quantity, quality and retention of manpower is one of the prongs of incremental growth.

Depth of engagement

The greater the incremental business a company gets from a given client, the more predictable its revenue gets. It is known that acquiring new customers is costlier than growing through existing customers (Pfeifer, 2005). Sunil Gupta, Lehmann, & Stuart (2004) find that a 1% improvement in retention, margin, or acquisition cost improves firm value by 5%, 1%, and 0.1%, respectively. They also find that a 1% improvement in retention has almost five times greater impact on firm value than a 1% change in discount rate or cost of capital. Therefore it is better to increase the depth of engagement with existing customers rather than scout for new ones. However what matters to customer retention in different domains is different. Gatignon and Xuereb (1997), for instance, conclude that firms should be consumer- and technology-oriented in markets in which demand is relatively uncertain. In the IT domain where product obsolescence is high, consumer needs shift rapidly (Gordon, 2009). This presents a challenge in retaining existing customers and increasing the depth and breadth of engagement. In Infosys, 80% of the revenue is contributed by 100 of their 600 clients (Interview with S Gopalakrishnan, 2011). Wipro won the Nasscom process innovation award for 2009 for its Cigma initiative which it claims has improved its depth of engagement with customers (http://outsourceportfolio.com/). HCL has signed a 5 year contract with Merck to streamline their operational efficiencies and consolidate their information technology (hcltech, www.hcltech.com). Other SWITCH firms are also signing long term contracts to deepen their engagement.

Reusable components/Solution accelerators

The service marketing mix consists of the 7Ps, namely, product, price, place, promotion, people, physical evidence and process (Booms and Bitner, 1981). Of these the last three elements are of specific importance to services because services firms often do not have control over the product (e.g. IT service companies have no control over hardware because it is manufactured by other IT companies, though they can pick and choose). Among these, process is separately listed as an important prerequisite for running a successful service (Yap and Sweeney, 2007). In fact some companies have successfully adapted processes from other industries like the Toyota lean manufacturing process to software (Hamm, 2007). Processes can and should be improved by inputs received from employees, customers, suppliers and intermediaries. When employee suggestions are implemented, organisational costs tend to go down (Arthur and Huntley, 2005). While the software requirements for different customers are different, there are elements of commonality that can be standardised. With minor modifications, large pieces of software code can be re-used because the methodology is largely the same as is the desiredfunctionality. Such standard modules of software are called solution accelerators or reusable components. Indian IT companies are developing standardised templates for specific industries so that they need not write code for big projects from scratch (Indian Rivals, 2010; Sharma, 2010). TCS has over 50 Centres of Excellence which track domain and technology trends and address the most critical client needs through specific frameworks or methodologies that accelerate the implementation process for third party products (www.tcs.com). HCL is part of TI's elite design house to write solution accelerators for aerospace, medical and consumer electronics (HCL Technologies, Accord Fontech, 2010).

Training employees for transformation

With software companies emphasising non-linear revenue, employees will have to not only work smart but also differently. For instance, more employees will be engaged in consulting work which demands an understanding of the business problems of customers rather than coding. Such ever-increasing demands on expertise call for a wide knowledge base (Sauser, 2000). They demand a wide variety of academic, technological and social skills and grounding in diverse disciplines and capabilities. It is such educational diversity that enhances information use and thereby makes information processing more efficient (Dahlin, Weingart, & Hinds, 2005). For this reason bulge bracket consultancies hire bright young MBAs from diverse disciplines (O'Shea and Madigan, 1997). Cognizant, head quartered in the US and modelling itself after the big five consultancies, has been hiring MBAs for several years now. The other Indian IT outsourcing companies have also been aggressively recruiting senior consultants from global consulting firms. Even straightforward coding to specifications is not easy as outsourcing is done across boundaries. Nuances in cross culture communication can create difficulties. For instance, while American contracts are explicit, Japanese tend to be more implicit. Therefore staffing, training and relationship management are the key drivers for success in software projects (Krishna, Sahay, & Welsham, 2004).

Cloud computing

An IT solution delivered to a customer is used only by his/her organisation. However a solution put on cloud can be shared by several customers. It saves the effort of coding and adds to non-linear revenue. The research firm IDC predicts that spending on public IT cloud services will grow more than five times the rate of the IT industry in 2011, up 30% from 2010. Besides social software, gamification and consumerisation have been identified as the big themes for cloud applications in 2011 (Lev-Ram, 2010). On-demand enterprise software revenue will break the $10B barrier compared to the global packaged enterprise software application market at about $90B. Cloud has moved from near zero to 90,000 virtual computers created per day on Amazon. It allows developing countries to use the infrastructure already available on the cloud without sinking money themselves (www.economist.com). SWITCH companies have announced big initiatives on cloud computing. Profit margins on cloud however, are low compared to brick and mortar products. Thus what value is offered on cloud and how it is offered is crucial to profitability. TCS has configured an SME cloud for firms in the Rs 50—500 crore revenue band (TCS bets big on 'SME Cloud', 2011, Business standard, 2 Feb 2011). Infosys, with well trained people and processes, claims to give substantial savings through cloud based offerings (Eluvangal, 2010). Each of the SWITCH companies is finding its way of adding value on the cloud.

Delivery for all stakeholders

The long term prospects of an organisation depend on its ability to create value for all stakeholders. (In the course of one of the author's programmes, the executives of a leading enterprise application software firm said that for every dollar the company earned, many more dollars were earned by the partners!) In IT unless the ecosystem benefits as a whole, an innovation will not achieve scale. In fact in IT, the stakeholders go beyond other collaborating companies and'Porter's Five Forces' (Porter, 2008). They also include third party developers, open communities, educational institutions, solution brokers, R&D establishments and universities (Nikolov and Ileiva, 2004; Parker and Pohlmann, 2007). The founder of Acer concurs when he says, 'Indeed, executives have to ignore what works best solely for themselves and give the idea of benefiting others precedence over their own interests. They themselves can thus benefit the most. This philosophy is similar to that of an ecological system, which can be sustained by interdependence' (Lin & Hou, 2010). When the big IT companies like IBM did not take the initiative to improve the Industry Standard Architecture (ISA) bus, a chip maker like Intel seized the opportunity. Prior to that, since the bus was slow everything from the hardware to graphics ran slowly. By erecting an eco system that benefited everybody Intel co-scripted the PC revolution with Microsoft (Gawer & Cusumano, 2002). When a typical service provider like TCS or Infosys provides a solution on the cloud, other companies like Amazon or IBM might provide the cloud services. Thus Infosys's solution will find acceptance in the market only if all the stakeholders benefit from it. This demands that the hardware providers, the application providers, collaborating Internet or telecom companies and finally the service provider act in unison.

Taking over a department

Outsourcing generally brings efficiencies to the outsourcer (Amaral, Anderson, & Parker, 2011; Bertrand, 2011). It traditionally meant hiving off non-core aspects of the business to an entity that could deliver the same economically and save costs (Clott, 2007). At the least outsourcing means voice business process outsourcing (BPO) work. However as the interaction matures the service provider takes over an entire department of the client organiaation or even runs the department for the client. This would change the way client companies work, reconfiguring their business processes, work flow, functions and departments (Contractor, Kumar, Kundu, & Pederson, 2010). SWITCH companies, of course, are keenly aware of the limitations of outsourcing. They cannot forever depend on the low cost advantage because companies from other countries like Philippines are aggressively competing for BPO work. The Philippines in 2010 earned $5.7 billion for call centre work from the US, Europe, and Australia compared to the $5.5 billion of India's call centres, according to the Everest Group, an outsourcing advisory firm (Srivastava, 2010). China is also playing for a greater share of the outsourcing pie (Flinders, 2009). Therefore SWITCH companies are trying to move to the higher end of the service spectrum. Infosys and Wipro are racing to broaden the services they offer and compete for higher-level work that usually goes to larger rivals including IBM, HP and Accenture. They are aggressively pursuing on-site work like managing companies' entire IT departments, networks and help desks (Sharma and Worthen, 2009).

Nuanced pricing

There are many different ways of pricing an IT service. The three well known methods are those based on time and material, fixed cost, and risk-reward sharing. In the first type of pricing the service provider charges based on the man-hours spent on the project. In the second, the overall cost of the project is fixed. In the third, the service provider gets paid based on the gains the client gets from implementation. There are also hybrid models of the three. Czerniawska (2003) feels that consultants are yet to prove their worth on risk-reward sharing and therefore 50% of the contracts continue to be time and material based (Clott, 2007). Recent research in outsourcing IT contracts shows that the link between project parameters, pricing and profitability is more subtle than is imagined. In general clients prefer fixed cost pricing to time and material pricing. But the SWITCH companies may have reasons to prefer the latter. Other things being constant, time and material contracts lead to Rs 748,000 (roughly $16,000) more than fixed cost pricing. In repeat projects counter-intuitively there is less profit than is usually imagined. Thus there is a lot of scope for intelligent pricing of software projects (Gopal, Sivaramakrishnan, Krishnan, & Mukhopadhyay., 2003). Dolan and Simon (1996) point to several ways of adjusting price through addressing market segmentation, customer needs, competitive environment and several other such variables. Traditionally Infosys earned more margins than Wipro because it executeed more lucrative projects (www.wikinvest.com). Cognizant is able to price better with its two-in-a-box strategy where a delivery person and a client service executive are jointly responsible to a client. By addressing the customer needs better they have been able to get greater traction for both top line and bottom line.

Executing the same strategy differently

It often happens that the strategy is sound but the execution fails (Bossidy & Charan, 2002). A given strategy can yield different results. For instance, SWITCH companies have been recruiting employees in large numbers. But what sort of employees they recruit can make a difference to the ultimate performance of the organisation (Zeithaml & Bitner, 1996). If a given organisation recruits a greater number of consultants as a proportion of its employees it is more likely to aim for higher-order work. Which is why the revenue earned per employee is much higher for a Mckinsey than a typical SWITCH company (www.careers-in-business.com; www.infosys.com). Similarly while all SWITCH companies might adopt cloud, what they deliver on cloud can be different. Infosys entered the infrastructure business relatively late but since they adopted an asset light strategy the move locked up fewer resources and eased profitability. Each of the SWITCH companies might be pursuing blue ocean initiatives (Chan Kim and Mouborgne, 2005) but what each of them treats as blue ocean might be different. For instance, Vineet Nayar, the CEO of HCL Technologies treats people, ideas and mindset as blue ocean 'droplets' (Nayar, 2010).

Initiatives for disruptive growth

Disruptive initiatives are more difficult to implement than incremental initiatives. Developing a brand or a product IP is more challenging than running a client department. So also acquiring consulting skills needs a change in method, mindset, processes and people. Similarly acquisitions are more a marriage of culture than convenience. These initiatives require fundamental changes in the way the organisation functions. However, when implemented over the long term they tend to yield results with an order of magnitude difference. We discuss below the following disruptive initiatives namely branding, product IP, consulting and acquisitions.

Branding

Kapferer (2008) believes that brand is a name that influences the buyer. There is also general consensus that a stronger brand can charge a higher premium (Aaker, 1991; Ailawadi, Lehmann, & Neslin, 2003; Keller & Lane, 2003; Leuthesser, Kohli, & Harich 1995). Aaker (1996) opines that there are four components to a brand namely, brand as product, as organisation, as person and as symbol. While IBM is seen as an end-to-end brand on the brand as product dimension, SWITCH companies might be seen basically as IT service brands. However, if among the SWITCH companies some brands are stronger than others, they can charge a premium. TCS is the oldest brand. Thus it has been able to deliver more projects than the others. Its global footprint is wide and deep. Infosys, on the other hand, is seen as a strong brand. Wipro is seen as strong in'telecom' while Cognizant is strong in the health domain. Each of these companies can therefore charge a premium in their respective domains of strength. This contributes to non-linear revenue.

IT service companies traditionally did not focus on product. Krishnan, Kriebel, Kekre, & Mukhopadhyay (2000) show that more capable personnel, adequate deployment of resources at the design stage and better software development process result in better software products. Michael Cusumano (2004) in fact suggests that it is good for all product companies to have services and all service companies to have products. Fang, Palmatier, & Steelkamp (2008) believe that the impact of a firm's transition to services on firm value (as measured by Tobin's q) remains relatively flat or slightly negative until the firm reaches a critical mass of service sales (20%—30%), after which point they have an increasingly positive effect. Bajaj (2009) gives reasons why India is slow on developing IT products. However companies like Infosys and TCS do have finance products. Infosys is trying to acquire product IP in mobile applications. Traditionally it was difficult for service companies to acquire IP because the IP rests with the customer. Now they are finding interesting ways to share IP with clients. Infinite Computers, an Indian IT outsourcing company, for instance, has the highest IP based revenue among the mid-tier IT firms (IIFL Report, 2010). This gives them licence income which is independent of effort.

End-to-end consulting

Consulting can be a difficult business because a consultant cannot canvass his own service and is dependent on referrals. Professional services (like consultancies) apprehend that any attempt at aggressively marketing their service might bring down their reputation and consequently harm their business prospects (Bloom, 1984). Contrary to what is expected, consultants not only need to work with clients but also with each other. This is because clients seek more than one opinion on important problems, often paying more for the second opinion (Sarvary, 2002). According to Czerniawska (2003) most big projects involve multiple vendors. Further, most research is agreed that the reputation of the consultant plays an important role in selection as well as post delivery satisfaction. Hill, Garner, & Hanna (1989) confirm the view and show that the knowledge and comfort dimensions are the most important selection criteria for choosing a professional service provider. Complementing this view, Brown and Swartz (1989) believe that inconsistencies in expectations lead to poor service experiences. While all SWITCH companies would like to do business consulting, it is more difficult to deliver than IT implementation. However, they are now recruiting aggressively from big consulting firms though they could still take time to establish credibility. Business consulting requires deep domain knowledge which the SWITCH companies are now acquiring. If SWITCH companies do acquire expertise in business consulting and domain expertise, they can enhance their non-linear revenue and also pose a significant threat to pure business consulting companies in future.

Acquisitions

Tsai and Esingerich (2010) classify internationalising firms into four types a) multinational challengers b) global exporters and importers c) Original equipment manufacture (OEM)/Original design manufacture (ODM) technology leaders and followers, and d) regional exporters and importers. They argue that overseas expansion of firms from emerging economies can be driven by their search for resources and other critical assets, such as technological know-how, R&D capability, managerial skills, and global brands to compete with their peers from developed markets. SWITCH companies today have reached the scale of multinational challengers though they started as global exporters. They are acquiring companies globally to expand their geographical spread and skill base. Turnbull and Doherty-Wilson (1990) point to mergers and acquisitions as one way of rapidly acquiring a global footprint. However, acquisitions do not always work well (Porter, 1987). Rankine (2001) identifies flawed integration management as one of the important reasons for the failure of acquisitions. Among SWITCH companies Infosys has been relatively cautious in its acquisitions while the others have been more aggressive. However, most SWITCH company acquisitions have been small companies that add incrementally to revenue and headcount. SWITCH companies have also not made hostile acquisitions. Their acquisitions have generally been niche companies that give them geographical reach and domain footprint.

Conclusion

SWITCH companies appear to be pursuing incremental strategies more than disruptive ones. That is possibly because they do not want to upset the steady growth they have experienced in the last decade and a half. If they do succeed in their strategies they can end up as strong competitors, not just to end-to-end IT firms but also pure play consultancies. This will give them another decade of growth or more. Disruptive initiatives however need courage and commitment. If they are successful in their new initiatives (incremental and disruptive) they can define a new business layer between IT and consulting by delivering it in their unique way.

The Infosys Experience: In Conversation with S Gopalakrishnan, CEO and MD, Infosys Technologies

S.Gopalakrishnan is one of the founders of Infosys Technologies Limited, a global IT business solutions provider headquartered in Bangalore, India. In 1981, Gopalakrishnan, along with N.R. Narayana Murthy and five others, founded Infosys Technologies. Between 1987 and 1994, he headed the technical operations of KSA/Infosys (a joint venture between Infosys and KSA at Atlanta, U.S.) as Vice President (Technical). In 1994, Gopalakrishnan returned to India and was appointed Deputy Managing Director of Infosys.
S.Gopalakrishnan served as the Chief Operating Officer from 2002 and as the President and Joint Managing Director from 2006 before being appointed as CEO and Managing Director of Infosys in 2007.
Recognised as a global thought leader, S. Gopalakrishnan was awarded the Padma Bhushan, the country's third highest civilian honour, by the Government of India in January 2011.

YLRM: In a recent interview you said that the non-linear revenues for Infosys for this year were about 4% and that they are likely to go up 10% in the next year. What are the various initiatives that you have on the non-linear side?

SG: Currently the non-linear revenues account for about 10% of the revenues if I include the product Finacle, which in some sense is non-linear. We want non-linear revenues to account for about a third of our revenues in future. We have not set an end date because this is more of a direction than a specific goal and it's a multi-year goal which we will recalibrate as we go along. As we continue to grow we have to look at a mechanism by which we can create a discontinuity between the number of people we employ and the corresponding revenue we get. Non-linear growth is one such mechanism and there are multiple ways in which we can do it. First of all there is a technology trend around cloud computing and IT businesses appear geared to be moving in that direction. By providing our solutions on the cloud, we can actually create a non-linear engagement model with our clients, because we will then compute the revenue based on the transactions delivered, the number of employees and so on. The second way is by pricing our existing services differently. Today when we fix prices on our maintenance projects or testing, the price is proportionate to the effort. In the future we are looking at pricing based on the number of tickets in the infrastructure management side, the number of devices managed and other such considerations. In consulting we are looking at outcome or output based pricing or value delivered. So for example, if we develop an application which increases the inventory turns, we would give our clients a base price and the premium based on results. We are looking at multiple ways in which we can change the trajectory and look at non-linear ways to grow.

YLRM: Let's take these initiatives one by one. For instance, if we look at cloud computing, at typical product companies like SAP, while there is an urgency to deliver through cloud mode, perhaps because of salesforce.com andother competition, there is also worry that their margins will reduce by half. The kind of money that they were making is because they are using their own product. In your case will you be delivering others' products and services? Or will it be your own?

SG: Let me answer the second one first. Yes, we are offering third party products as a service. In fact, we service offerings today based on Peoplesoft from Oracle, ERP from SAP. We have products also from other companies which we host and deliver as a service. The idea is that the value addition from Infosys must be significant on top of whatever is the underlying infrastructure, because even when we deliver our own products and services, the hosting is usually outsourced. We need to create an ecosystem of partners and this partner could be a product company or a hosting company but we want to make sure that our value addition is such that our margin requirements are met.

As for how much the margin is, is a function of the value addition we can make. If you don't make any value addition, if you provide a commodity service on the Internet, then our margin may come down. Granted that margin is the function of the market, but more importantly the margin is a function of the choices you make internally, such as the kind of a value addition you want, how you run your business, the services and products you want to enter into and so on. You can take any product andget different margins – for example look at the MP3 player; Apple makes an iPod and gets a significantly higher margin than somebody else. Brand is also important.

How you deliver is very important and determines what is the margin you will get.

YLRM: Let me give you an example and see if it fits. Would you take something typically available, a commodity such as CRM, and top it with analytics to add value ...

SG: Yes, we could do analytics and also run business process around customer service and so on. When we deliver HR outsourcing we are the HR department for the client company, we run all the business processes for them, take the responsibility for the licence cost and the maintenance cost of the application and we also take care of the infrastructure, including the physical infrastructure. So, the entire stack is delivered by Infosys. We may outsource the back end to some other companies or partners.

YLRM: One of the things you have not spoken about is acquisitions, which is another piece of growing non-linear revenue. While Infosys has been growing, compared with its peers it has been rather tentative and cautious in terms of how it takes over. Time and again your spokespersons have clarified that the acquisition should make top-line, bottom line and strategic sense for you to buy, which is why you have been somewhat tentative. Has it in some sense reduced the ability grow non-linearly?

SG: Acquisitions are inorganic ways in which you can grow and on the other hand there is organic growth. When we internally prepare our strategies, look at the business plan etc., we look at the organic piece and on top of that we put the inorganic piece. There is no assurance that we will find the right company at the right price with the right product and service. So it is not a predictable way to grow.

We don't want to be dependent on acquisition for our growth and organically we will try and grow as much or better than the industry, as we have been doing in the past. We have not lost out on growth and if we make an acquisition it will be over and above organic growth. We have a strategy around acquisitions. We have clear parameters that we have set for ourselves in terms of the size and the company we look for, specific areas, what kind of employees the company has so that we are able to integrate them – we want to retain 100% of those employees — and so on. We are not looking to acquire a failed company and fixing it. We are looking at a good company that will add value to the company and our customers and investors.

YLRM: You have been fairly tentative in this but the others have taken over companies fairly rapidly. Integration of people, processes and geographies is important. This has been something of a challenge for Indian companies, by and large. Would you say that it is true?

SG: It is not just the case with Indian companies. If you look at the history of acquisitions and the data from acquisitions, 70% of acquisitions do not deliver the value they are supposed to deliver. The rate of failure is very high. Indian companies have additional problems in terms of culture, distance, leadership styles, and so on. So all those things will have to be factored in when you look at an acquisition.

YLRM: The other aspect that you were talking about is consulting which most Indian companies are trying to do. What exactly is there in consulting which Infosys has not been doing so far or proposes to do more of in the future?

SG: There are two areas in which consulting would help an organisation. First is in the identification of the problem and second, in the definition of the solution. So what should the licencing model be, let's say for a software product company? This is a question typically a consultant would answer. Once you identify the licencing model, then you look at the system changes that are required in order to implement the licencing model in the organisation. Thus we would identify the problem, define, design and develop the solution, implement it, maintain and support it. So we have now end-to-end capability, all the way from consulting to running the operations of the company. This gives tremendous choice for our clients to engage with Infosys. They can engage at a very early stage, at the definition of the problem, or much later, wherever they are stuck. As we develop a strategic long term relationship with our clients we find that we are able to sell multiple services to the same client. We are able to help them with end-to-end services.

What we are not doing today but could do in the future is scaling. Our consulting service, especially business consulting, is a small piece of our overall business today. There is an operational consulting piece which consists of transformation around package implementation and so on, which is doing much better and is substantially large, contributing about 25% of our revenues. We believe that this can scale up significantly and as we become more strategic to our clients this is the scaling up we need to do. Infosys today has about 600 clients and about 100 clients give us 80% of our revenues, a 20:80 kind of a thing. We have a long way to go as far as growth is concerned and consulting is very important; we have to make sure that we can grow within these clients and add new clients.

YLRM: We get that Sir, but the issue is that consulting needs different kinds of skills. The vast majority of employees at Infosys has been and is on the IT side and now you are believed to be taking people on the consulting side as well. Other than the question of skills, which are certainly important, is it also a question of mindset in terms of how one addresses

business problems because traditionally one has not been addressing business problems but solving IT problems. None of the Indian companies has actually been addressing those problems in the past. Would you say that is a challenge?

SG: We are in three businesses. The first is helping companies change, transform. This is the area where consulting is helping and can help a lot. The second area is running business operations. Our IT department runs the IT operations for the client who outsources them to us. Even the applications development and maintenance is part of business process within an IT organisation. The third piece is innovation R&D, which involves helping companies with new products, new technologies and so on. By and large we were in the operations field till now and that required certain deliverables. Value addition to our clients means efficiency, meeting service levels, lower cost and so on. We have been hiring the right people to do that. Actually, the people are the same whether it is for transformation or consulting, the difference lies in the training, the business processes and the quality systems. So, 'mindset' to me is rather abstract. What is more important is the training that we impart and the people that we recruit. For any business we recruit people with learnability, problem solving skills, communication skills, the right attitude and things like that. So they will do equally well in consulting with the right training and the right set of methodologies, processes, tools, mentoring etc., Right now our focus has been on the operations piece so that the training, the tools and the techniques have been targeted towards that and we are doing a good job there. I don't see this as a big change given the type of people we recruit. It is how we enable them, equip them and deliver the service.

YLRM: So the piece you are looking at is the business-IT- consulting interface not business consulting per se.

SG: Business consulting also. Yes.

YLRM: Won't that need different kind of people with altogether different qualifications?

SG: When a person with an engineering degree does an MBA, what does it do? It gives him the technique and the tools for doing consulting. Building on his engineering, he is being equipped with a set of new tools and techniques.

YLRM: Let us look at the other piece we were talking about – product IP. Typically, software resides with the client with whom you are doing business and so also the IP. So if you want to do something interesting on the product you licence it to the client. How will you create product IPs? There is some buzz to the effect that Infosys is doing something in this direction.

SG: We have been doing product IP for a long time. Finacle, a core banking product from Infosys has been existing for 25 years. It started in 1985 and is used by 75% of the leading banks in India, now deployed in multiple countries around the world. It is one of the top three universal banking products in the world today. So we have been able to create a world class product out of India, and we can scale it up and grow. Now we are investing in creating IP solutions and licencing it to the client. That's the third piece I talked about.

When we look at our business in future we look at it as the 'transform' piece where we help our clients with their changes. Second is the 'operate' piece where we help run their business. The third is the 'innovate' piece where we help with IP, with solutions, with products, with platforms and so on. You will see us investing heavily in the third piece as well.

YLRM: Finacle has had its ups and downs, hasn't it?

SG: Yes, the business model, the investments patterns, the branding required, the sales and marketing model are all different. Finacle is focused on selling the licence to as many clients as possible, so you need to create a partner ecosystem of people who can instal it, support it and so on. Infosys is one of the system integrators of Finacle; one of our competitors could also integrate Finacle. So, the business model is very different. It has its own sales team and marketing team.

YLRM: Again, it needs a different kind of approach. You need to invest upfront, and sometimes the risk is higher. As of now I think it forms a small part of the revenues (3—4%) but you wouldn't probably want to give a number on how far you want to go.

SG: We have a directional statement that a third of our business should come from transformation, a third from operations, and a third from IP. That will include the cloud based services which could be giving us a predictable revenue stream as those services are based on an annuity revenue stream. (When a product is licenced as an annuity revenue model, then you get a continuous revenue stream.) Many product companies today are moving to a subscription model. A product can be licenced in a subscription model.

YLRM: Yes, all this is being done by Indian companies. The non Indian, i.e., American companies have also been increasing their footprint in India. There is pressure on them to bring down costs because of the challenge thrown by Indian companies. On the other hand, the salaries on the Indian side have been going up. At some stage, is there a point of difference? How do we give something that an IBM or an Accenture can't give? Is that a consideration?

SG: Yes and No. The differentiation between Indian IT services companies and global IT services companies is reducing. All of us are becoming similar in the way we deliver the service part, because all of us are using the global delivery model to deliver the service. The differentiation will come from the customer experience, your track record of project execution, your track record in terms of the ability to scale up and support your clients, in terms of anticipating the changes in the industry and making those changes on the vision and strategy part and things like that. Indian IT services companies had a particular trajectory. They will have to take a different trajectory when their competition is not other Indian companies alone, but global. But from day one, our competition was global. The only thing we had was the cost advantage. Now the same cost advantage is available to others as well. This has become the mainstream model and whoever executes the model better, anticipates the trends in the industry and makes the necessary changes will ultimately win. So, Indian companies are much larger, stronger. They have a good track record, profitability, cash, the market cap and everything else, which is a far cry from what they had 20 years ago. I believe we are in a better position to compete today than we were 20 years ago.

YLRM: Absolutely, there is no question there. What you said is certainly true of the service side. However, in the relatively new initiatives like consulting and so on, would you still say they are comparable?

SG: No, in consulting foreigncompanies have a bigger base of clients, bigger relationships and a bigger track record. When you venture on something new, you have to disrupt the existing model and deliver. Let me take a different example, infrastructure management. When we introduced that service we introduced it as an asset light model. We said we will not own the infrastructure model to control and manage the infrastructure. It was new to the industry. But today we have succeeded in creating a new space for ourselves and we are considered leaders in that space. Ours is one of the largest infrastructure management practices in India today. Hence, when one comes into the picture much later, like we did, one has to do it differently. What is our value proposition in consulting? We say that we stand behind what we recommend and we implement what we recommend. The challenge in consulting is that a report or recommendation given to the client is useless if it can't be implemented or is poorly implemented or never implemented. We guarantee that what we recommend can be implemented; we will stand by the cost and the time frame. So you get certainty and predictability and that's resonating very well with our clients, because usually execution track record is poor. And execution is our strong point.

YLRM: To come back to the point where this discussion started, how do companies increase non-linear revenues? Which means make it man power independent. But if we consider implementation, then it can never be man power independent.

SG: Let me correct that, in the sense that generating non-linear revenues is not an imperative. It is a good thing to have, a smart thing to do, but it is really not an imperative. As we grow and look at new engines of growth, as we look at trends in the market, like cloud computing, it makes sense for us to look at that piece. So the non-linear piece is something which we are consciously doing, not because we are forced to do it. In fact, internally I tell our people, if we have to grow linearly and for doubling our revenues we need 250,000 people, we should not have any hesitation. We just need to figure out the organisation structure that can manage 250,000 people. The wrong mindset is the biggest challenge any organisation or leader can face in making something happen. In our minds there should not be any bottleneck or fear of 250,000 people. Having said that, why not take advantage of something that we see in the market, why not create growth engines. It is something we are making a conscious choice to do.

YLRM: So in other words what you are saying is, this is an additional piece which is an interesting way of growing.

SG: Exactly!

YLRM: Otherwise you have no problem. You can keep ramping up.

SG: We can keep ramping up, we can increase the revenue productivity by making service selections, by growing in consulting and so on. These are choices we are making.

YLRM: How does an MNC which is located somewhere else, say, or abroad, differentiate between the different Indian IT service companies? All of them have their footprints with several of these clients. Some of these relationships are long term relationships. Given this, how does Infosys differentiate itself from the rest of the Indian companies? Are there any specifics it stands for?

SG: It is a multitude of things. It's the way we compete, the values, ethics, corporate governance and focus we have, our products and services, the industry segments in which we operate and how we compete in the market. We compete based on value, we don't compete on costs – we make it very clear to the client. Yes, we will be competitive in the long term. If you want rate per hour, ours will be higher. We are very open about it and we're a premium player. So every one of these things counts – our focus on financial services, on solution, on consulting and how we enter a market. We don't enter a market because somebody else is there, we enter a market because we believe we have certain strengths and unique value propositions. That is how we entered the BPO business – we entered late but we differentiated and we grew in that business. So also with infrastructure management. In the eyes of the clients there is clearly a difference and that's the reason why we're growing and we're a premium player in the market. When it comes to customers, it's about the solutions, the services, the IP, the predictability we bring in and the commitment to our clients. There is a certain basket of values we provide to our clients. For employees it's about compensation, learning, growth, working with a peer group that is respected in the industry, working in an open culture and so on. In terms of investors, it is corporate governance, high returns, predictability, sustained growth, leadership and a certain visionary outlook. There is a set of value propositions we bring to every one of our stakeholders and there is a difference. That is why we are a preferred employer, the company of choice, even in campuses. Our customers trust us with some of their most complex projects. Repeat business is very high and so is stickiness. From an investor's perceptive it is higher market cap and valuation.

YLRM: So essentially what you're saying is, these initiatives are common to anybody who wants to grow and other Indian companies are also taking them. You seem to be suggesting that your ability to stick to what you deliver is really what differentiates?

SG: No, it is how you execute, how you add value to your clients, the focus you have in delivering these services and the value you can bring to our clients. For example in consulting we were very clear from day one that our differentiation will be the ability to implement what we propose. So our delivery teams are there as part of the consulting team from day one, looking at implementation aspects, at technologies and the choices that the client makes. The proposal can be converted into a technology solution, the designers are part of the team that is delivered – we call it the One Infy solution. In fact we have a value realisation model which looks at how we justify the solution and if the solution was implemented what would be the outcome and so on. The business case for doing the work, implementing etc., is part of the consulting proposal or consulting report itself.

YLRM: So you are saying that doing the business itself differently and adding value to the client is really the differentiation. Sir, one last question. If you were to redo something completely and if you were given an opportunity to go back in a time machine and do that, is there something different you would do?

SG: Probably not, because we are successful. The only question to ask is could we have done it any faster and nobody can answer that. It's a hypothetical question.

YLRM: Thank you Sir.

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